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Economic Perspective

SUBSIDISE THE PRICE OF LABOUR, NOT THE PRICE OF ENERGY

by David Simpson, Fraser of Allander Institute*

Amongst the items which featured in this year's Budget, announced on 9 March, was a so-called "Industrial Energy Package". This contained proposals for paying subsidies to "larger industrial users" of gas and electricity. Together with similar measures announced in last year's Budget, these arrangements will benefit the firms concerned, (whose identity remains undisclosed) to the extent of £250 million. It is difficult to think of any justification for the payment of such subsidies. Certainly none was offered in the Budget statement other than that these unspecified firms "face the greatest difficulties".

These "larger" users are believed to be in the steel and chemical industries. It is argued by representatives of these industries that their products are placed at a disadvantage in international markets because the costs of electricity are higher in this country. They say that this is because a large part of electricity generation is coal-fired, and that the UK is a high cost producer of coal by world standards. This might be an argument for either moving away from coal as a fuel, or else substituting imported for domestic coal. It does not constitute a serious argument for subsidising electricity. Strangely enough it is also part of the "industrial energy package" to extend the existing scheme of grants towards the cost of converting oil and gas-fired industrial boilers and equipment to coal.

It is also alleged that European and other competing producers of steel and chemicals have their energy costs subsidised by their governments. If this is true, the correct response should be to import more steel, in order to gain the benefit for ourselves, as consumers, of these subsidies, in the same way that we benefit from foreign subsidies on imported dairy products and other goods.

Once this is recognised, it is easy to see that it would be better to spend the sums of money concerned on direct wage subsidies for those whose employment is threatened. But the subsidy should be attached to their wage, wherever they are employed, and not to any particular employment. Government ministers frequently talk of the need to price people into jobs, and, indeed some of the more successful job creation schemes are of this kind. It would therefore be consistent with the Government's declared policy to spend this £250 million on subsidising wages, not on subsidising energy prices.

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The fact that there is, at present, an excess supply of labour poses a serious human, as well as an economic, problem. The fact that there is an excess supply of energy poses no human problem at all. But few economists believe that the present glut of energy is anything but temporary. Most would agree that present energy prices are below their long-run trend value. In this case, it would make sense for government to tax, not subsidise, the price of energy. Indeed in this Budget, the government chose to increase the tax on petrol to household consumers: exactly the same logic should apply to industrial consumers of energy. Thus, on neither social nor on economic grounds, is there a case for subsidising energy, while, so long as severe unemployment persists, there are social as well as economic grounds for subsidising wages.

It may seem a simple matter for government to offer subsidies to a few firms. But the consequences are frequently very different from those intended. For example, the civil servants who arranged the massive, (but once again undisclosed), subsidy to Shell-Esso to encourage them to build an ethylene cracker at Moss Morran did not apparently take into account the damage which this might do to employment amongst their actual or potential competitors, such as BP or ICI. Nor did the other civil servants who arranged the disguised subsidies to the Anglesey smelter owned by Kaiser Aluminum Inc and RTZ Ltd consider what the consequences might be for competing producers such as the British Aluminium Co who operated the Invergordon smelter. The facts and figures concerning these agreements are always concealed by reference to considerations of commercial confidence, but it is reliably reported that a new operator for the Invergordon smelter would require an annual subsidy of £20 million, out of a total electricity bill of some £27 million. When it is realised that this works out at an annual subsidy of more than £20,000 per employee in the case of Invergordon, (and perhaps even more in the case of Anglesey), the irrationality of the whole exercise becomes patently clear. Worse still, even those civil servants who administer the subsidies, and who are privy to the confidential agreements, cannot know how much of these subsidies accrue to employees and how much is simply a free gift to the multinational companies concerned. Indeed, it would be interesting to discover the size of the undisclosed transfers of public funds to multinational companies operating in Scotland in the last twenty years.

Perhaps the most disquieting aspect of the whole question of subsidising energy prices is not simply that large sums of public money are being devoted to promoting private as opposed to public interests, contrary to the government's own frequently declared policies, but that all this takes place covertly, so that public accountability is impossible.